2016 Highlights

**Economy**
The unemployment rate of the Czech Republic in 2016 was the lowest in the EU. While it contributed to positive consumer confidence, it wasn’t such good news for employers as this increased pressures on wage cost.

**Investment Market**
Record volumes of investment into real estate (€3.8bn) were driven by both domestic investors and established foreign/new international investors entering the Czech market.

**Office Market**
Strong levels of net demand in 2016 (228 thousand sq m). Vacancy therefore continued to decrease (now at 10.6%), driven both by strong occupier demand as and record low levels of new office space completions.

**Industrial Market**
Gross take-up reached a new record high with 1.465 million sq m. Vacancy level dipped below 4.5%, encouraging new speculative development. However a large part of the pipeline was already leased prior to scheduled completion.
Economy

2016 OVERVIEW

- The growth of the Czech economy continued in 2016; at the end of Q3 the GDP stood at 1.9%.
- Czech CPI index grew at an increased pace towards year end, approaching the target (2%) set by the Czech National Bank quicker than was originally expected.
- The government budget for 2016 ended in surplus, i.e. 0.7% of GDP. However, this was partially achieved due to cuts in government spending and by the level of EU subsidies.
- Unemployment rate, in spite of minor fluctuations, remained the lowest in the EU and by the end of November was 3.8%.

OUTLOOK

- Robust economic prospects of Germany in 2017 are likely to translate into a solid 2.4% year on year (y-o-y) economic growth for the Czech Republic.
- We expect Czech average wage growth to be close to 5% (possibly higher in Prague) as the tight labour conditions of 2016 continue. Wage growth will therefore likely translate to further inflationary pressures.
- Czech CPI has been moving upwards recently and will continue to do so as the currency cap on the exchange rate with Euro is removed, ending 2017 at 3.0% or higher.
- The Czech Koruna base interest rate is likely to rise from its current level at 0.05% in 2017 towards the 1%-3% range.
- A moderate budget deficit of −0.8% of GDP is expected ahead of the Czech national elections scheduled for October 2017. Government investment is likely to increase y-o-y at around 2%.
In 2016, investment in the Czech real estate sector reached new record highs and by year end, more than €3.8 billion had been transacted.

The figures were helped by some exceptionally large deals: six deals were in excess of €100 million, with three of them consisting of only a single property.

Local investors dominated the market with a 30% share of total investment. However, we also saw new entrants with capital sources originating from countries such as China, South Africa, Singapore and Lebanon.

By share of total investment activity and number of deals, the office sector dominated in 2016 with 36 transactions and a 44% share.

By number of deals, industrial was subdued but there was one notable transaction, i.e. the sale of the P3 European Industrial Platform to GIC (Singapore). A significant portion of this portfolio being located in the Czech Republic.

Due to increased investor demand, prime yields compressed throughout 2016 and also across all market segments, reaching new cyclical lows (see chart).

Our outlook for 2017 remains positive, with a number of transactions in the pipeline. Some of these transactions comprise investment deals in excess of €300 million.

Czech commercial property will continue seeing increased demand, underpinned by the popularity and liquidity of the market. We do not however expect much further tightening of prime yields, given bond yields moving out and the spectre of future interest rate rise in the EU and the Czech Republic being a possibility.
SUPPLY & VACANCY

By the end of 2016, total office stock in Prague reached 3.24 million sq m.

During Q4 itself, only one smaller property was added, bringing total completion volumes in 2016 to 33,400 sqm, the lowest completion level in the city’s history.

Low level of completions was one of the factors contributing to a vacancy drop: by year end, the vacancy rate in Prague reached 10.6% while at the start of the year it was 14.6%. A similar low vacancy level was last recorded back in Q3 2009.

Out of current vacant stock (339 thousand sq m), some 62% was accounted for by office properties older than 10 years.

DEMAND

Although gross office take-up (411 thousand sqm) was 10% lower than in 2015, net take-up reached 228 thousand sq m, 6% above its 2015 level and the highest recorded yet in Prague.

Annual net absorption has also been in the positive territory for each of the past six consecutive years.

PIPELINE

By the end of Q4, more than 330 thousand sqm of new modern offices were under construction with completions scheduled between 2017-2018. Almost a quarter of these office premises were already been pre-let.

Furthermore, a number of projects were in preparatory phase; therefore, we expect the development pipeline for 2018 and thereafter to increase.

In our view, office vacancy is likely to continue decreasing until Q3 2017, when some larger office development projects hit the market. Thereafter we expect some minor escalation in the vacancy rate.
SUPPLY & VACANCY

- By the end of 2016, total industrial warehouse stock in the Czech Republic reached 6.26 million sq m.
- In 2016, Czech industrial stock grew by 9% with some 501 thousand sq m of new space delivered.
- The country average vacancy rate by the year end was only 4.75%. Vacancy levels did however differ significantly between regions: e.g. from zero in smaller regions (where so far build-to-suits have prevailed) to 15% in say the Pardubice area.
- Prague with 2.48 million sq m of warehouse space was by far the largest industrial hub in the country, accounting for 40% of total stock.

DEMAND

- Gross industrial take-up reached 1.465 million sq m, which was the best result in the market’s history, however only actually exceeding the 2015 figure by 1%. In terms of net take-up, 2016 did however show a y-o-y dip of 5%.
- The year ended strong with Q4 delivering the strongest leasing results in the market’s history, with 510 thousand sq m of deals for three months.
- Not surprising given such a low vacancy environment, 37% of all leasing deals in 2016 were actually pre-lease agreements.
- Prague dominated take-up: 46% of gross take-up and 35% of net take-up targeting the area in or around this capital city.
- For occupiers seeking larger space (>5,000 sq m), only 16 warehouses really offered such availability across the whole country. Six of these comprised space in new project completions in 2016.
- Low vacancy rates are increasing opportunities for rental growth and we already see some landlords asking rents of around 10% above their previous benchmark headline rent.
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